

CIA/OER/S-06638-74 PERU: CURRENT ECONOMIC SITUATION AND PROSPECTS CONF

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25 November 1974

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MEMORANDUM FOR: Chief, [REDACTED]

SUBJECT : Peru: Current Economic Situation
and Prospects

In response to your request, we are transmitting
the attached briefing paper which was prepared for use
by the [REDACTED] in briefing certain Peruvian
officials on the state of the economy. Questions may
be directed to the author, [REDACTED], x1516 Red.

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Chief,
Latin America Branch
Office of Economic Research

Attachment:
As stated

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Peru: Current Economic Situation and Prospects

I. Peru's economic situation has worsened slightly in 1974 compared with a year earlier.

- A. Real GDP growth has slipped to 5.0% from 5.8% in 1973.
- B. Industrial production has dipped a little.
- C. Mining output and exports have stagnated.
- D. Agricultural production remains low, contributing to sporadic shortages of basic foodstuffs; peasant opposition to cooperativization and other agrarian reform problems continue to hold back farm output.
- E. Private domestic investment continues to be discouraged by social reforms.
- F. The inflation rate probably will reach about 25%, up from 14% last year; rising import prices and an increased government deficit are the responsible factors.
- G. Rising import costs for food and oil may put the 1974 trade balance in the red despite increased fishmeal exports and greater earnings from copper exports because of high prices.
- H. Despite increased private capital inflows for oil and copper development, the 1974 balance-of-payments surplus accordingly will be a little smaller than last year.

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II. Increased availability of anchovies has brought improvement in the fishmeal industry compared with last year.

- A. As a conservation measure, the government has limited the anchovy catch to 5 million tons, up from 1.8 million in 1973...
- B. Fishmeal production will reach about 1.1 million tons, with an estimated amount available for export of 900,000 tons, compared with 350,000 tons last year.
- C. Weak demand for fishmeal forced Peru to reduce the price from \$400 per ton to \$270 per ton at mid-year. Earnings in 1974 will total about \$250 million, up from about \$140 million in 1973.
- D. Earnings are likely to grow steadily as production increases over the next several years; barring a return of El Nino, they should reach about \$400 million by 1976.

III. Per capita food production of basic foodstuffs continues to decline while large tracts of expropriated land lie idle as the government ponders how best to implement its agrarian reform program.

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- A. In the 1974-75 crop year, Peru will be forced to import about 900,000 tons of wheat, 375,000 tons of corn, 100,000 tons of sorghum and about 75,000 tons of rice.
- B. The government's 1975-78 National Development Plan is aimed at expanding food production and curtailing dependence on imports. Emphasis will continue on agrarian reform and expansion of irrigation, credit, and research facilities. To spur production, the Agricultural Bank has established a 3-year, \$37 million rural credit program with financing from the World Bank and IDB.

IV. Peru's already large government deficit will increase substantially this year.

- A. Consumer subsidies for food, power, and oil will rise to an estimated \$320 million, or 9 percent of the budget.
- B. Growing pressure from organized labor will force the government to grant public sector employees a moderate salary increase before year end.
- C. Despite probable tax increases and other measures, the deficit will continue to grow as the government is forced to assume increasing responsibility for financing economic development.

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V. Foreign and domestic investment in industry continues to be discouraged by the regime's social reforms.

- A. Recent legislation such as the Industrial Communities Law and the Social Property Law, which require businessmen to turn over substantial equity shares to their workers, has made industrial investment extremely unattractive.
- B. Both foreign and domestic investors have been further discouraged by President Velasco's National Day speech in July, which left little doubt that the military government intends to nationalize most sectors of the economy.
- C. The low level of private investment will force the government to assume responsibility for industrial investment, in time contributing heavily to budgetary problems.

VI. Despite the dismal investment climate, foreign capital probably will still be forthcoming for oil and copper expansion.

- A. Thus far, about \$456 million has been committed for the construction of the \$500 million Transandean pipeline.
- B. Principal commitments include a much-publicized \$230 million loan from Japan, a \$100 million

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Iranian loan, a \$44 million loan from Argentina, and \$43 million from West Germany.

C. Recent government actions, however, are jeopardizing the financing for the \$650 million Cuajone copper mining project, more than 60 percent of which had been assumed to be certain. The state mining agency, Mineroperu, has now proposed a variety of changes in advance sales contracts that had been scheduled to be signed in late September. The signing of these contracts is a prerequisite for a \$200 million loan package being supplied by a 52-bank consortium headed by Chase Manhattan.

VII. Copper exports in 1974 remain at last year's level, tons about 200,000/ but earnings are well above last year.

A. At this year's probable average price of 93 cents per pound, copper earnings will amount to about \$410 million, up from \$285 million in 1973.

B. Earnings are likely to drop to about \$240 million next year as weakened copper demand in the developed countries makes a price range of 55¢-60¢ per pound likely. Export volume probably will not increase before 1976 when three new mines -- Cuajone, Cerro Verde, and Santa Rosa -- are scheduled to start producing.

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VIII. Peru will remain dependent on oil imports at least through mid-1977

- A. Total consumption, now about 110,000 bpd, exceeds production by about 35,000 bpd.
- B. Jungle exploration thus far has resulted in establishment of about 22 producing wells with a capacity of 50,000 bpd.
- C. Pending the completion of the Transandean pipeline, lack of transportation to the coastal areas hinders use of jungle crude. The government insists that the pipeline will be completed in 1976 but a more realistic expectation would be late 1977 or even early 1978.

IX. The 1974 balance-of-payments surplus will be much smaller than originally anticipated.

- A. Growing imports of more costly wheat, feedgrains, vegetable oils and petroleum may produce a small trade deficit this year, as opposed to a \$90 million surplus in 1973. Food and petroleum alone will cost an estimated \$315 million.
- B. Expected capital inflows for the Cuajone mining project and the Transandean pipeline probably will exceed \$500 million this year and will offset the

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trade deficit and rising external debt payments. Because of the dismal foreign investment climate, other foreign investment seems unlikely.

C. Since oil exports are unlikely by mid-1976 as previously scheduled, the period of coverage of the government's development plans by external borrowing is correspondingly extended. Thus the burden of debt repayments, already at 23% of export earnings, will continue to mount.

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